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No. 87-1043

In The
Supreme Court of the United States
October Term, 1987

UNITED STATES OF AMERICA,
Petitioner,
v.
RON PAIR ENTERPRISES, INC.,
Respondent.

RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

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QUESTION PRESENTED

Whether Section 506(b) of the Bankruptcy Code (11 U.S.C.) & (Supp IV) entitles a non-consensual lien creditor to receive post-petition interest on an over secured claim in a bankruptcy proceeding.

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Ron Pair Enterprises, Inc., by its counsel I. William Cohen, Esq. and Michael H. Traison, Esq. of Hertzberg, Jacob & Weingarten, P.C., opposes the petition of the United States of America for a writ of certiorari to review the judgment of the United States Court of Appeals for the Sixth Circuit in this case.

OPINIONS BELOW

Respondent adopts Petitioner's statement of the Opinions Below.

———o———

JURISDICTION

Respondent adopts Petitioner's statement of jurisdiction.

———o———

STATUTE INVOLVED

Section 506 of the Bankruptcy Code (11 U.S.C.) & Supp. IV as set out in Petitioner's statutory appendix to its petition.

———o———

STATEMENT OF THE CASE

Respondent adopts Petitioner's statement of the case as stated in its Petition.

———o———

ARGUMENT

Respondent agrees that the decision of the Court of Appeals for the Sixth Circuit concerns a significant bankruptcy issue and that its decision directly conflicts with the decision of another court of appeals. Respondent concurs that the question presented is a frequently recurring one that is of considerable administrative importance.

However, the Court of Appeals for the Sixth Circuit decided this case correctly, had the benefit of the erroneous decision of the Court of Appeals for the Fourth Circuit when considering its decision and distinguished it. The Supreme Court should not disturb the decision below.

The Bankruptcy Court and the Court of Appeals for the Sixth Circuit correctly relied on cases decided before and after the enactment of the Bankruptcy Code. It is clear that 11 U.S.C. Section 506(b) is intended to codify pre-Code law prohibiting the payment of post-petition interest on pre-petition non-consensual lien claims. Nothing in the legislative history indicates that 11 U.S.C. Section 506(b) was intended to overrule the long standing prohibition against paying post-petition interest on pre-petition non-consensual lien claims.

The general rule in bankruptcy and other insolvency proceedings is that interest ceases to run on secured and unsecured claims with the initiation of the proceeding, i.e., the filing of the petition. *Vanston Bondholders Protective Committee v. Green*, 329 U.S. 156 (1946); *City of New York v. Saper*, 336 U.S. 328 (1949); *Sexton v. Dreyfus*, 219 U.S. 339 (1911).

As the Supreme Court in *Thomas v. Western Car Company*, 149 U.S. 95 (1893) explained:

> Exaction of interest, where the power of a debtor to pay even his contractual obligations is suspended by law, has been prohibited because it was considered in the nature of a penalty imposed because of delay in prompt payment—a delay necessitated by law if the courts are properly to preserve and protect the estate for the benefit of all interests involved . . . As a gen-

> eral rule, after property of an insolvent passes into the hands of a receiver or of an assignee in insolvency, interest is not allowed on the claims against the funds. The delay in distribution is the act of the law; it is a necessary incident to the settlement of the estate.

Historically governmental entities' claims for past due taxes received special treatment, accruing post-petition interest until the date of payment. See *City of New York v. Saper, supra.* In *Saper*, however, the Supreme Court held that the general prohibition against the payment of post-petition interest also embraced tax claims in bankruptcy cases.

> The Court of Appeals concluded that by the 1926 amendment and the Chandler Act, Congress assimilated taxes to other debts for all purposes, including denial of post-bankruptcy interest. We think this is a sound and logical interpretation of the Act after those amendments to 64(a) and 57(n). Considered in conjunction with the general rule against post-bankruptcy interest as well as 63's limitations of interest on other claims to date of bankruptcy, they compel our conclusions, already stated, that the *statute as amended did not contemplate any exception in favor of tax claims.* (Emphasis added).

336 U.S. at 338.

Saper's ban on post-petition interest for tax claims has been extended to Chapter X Reorganizations, *United States v. Edens*, 189 F.2d 876, 877 (4th Cir. 1951), *aff'd per curiam*, 342 U.S. 912 (1952); Chapter XI Arrangements, *Commonwealth of Massachusetts v. Thompson*, 190 F.2d 10, 10-11 (1st Cir. 1951), *cert. denied*, 342 U.S. 918 (1952); *United States v. General Engineering and Manufacturing Co.*, 188 F.2d 80, 81-83 (8th Cir. 1951), *aff'd per*

curiam, 342 U.S. 912 (1952) and Section 77 railroad reorganizations, *In re New York, New Haven and Hartford Railroad Co.*, 304 F.Supp. 1121, 1129-32 (D. Conn. 1969).

Following *Saper* the Government attempted to have the courts confine that ruling to pre-petition tax claims not reduced to liens. Three District Courts were not so persuaded. *In re Industrial Machine & Supply Co.*, 112 F.Supp. 261 (W.D. Pa. 1953); *In re Lykens Hosiery Mills*, 141 F.Supp. 895 (S.D. N.Y. 1956) and *In re Cameron*, 166 F.Supp. 400 (S.D. Cal. 1958). *Contra In re Parchem*, 166 F.Supp. 724 (D. Minn. 1958); *In re Ross Nursing Home*, 2 B.R. 496 (Bkcy. E.D. N.Y. 1980).

As previously stated, the IRS grounds its request for post-petition interest on 11 U.S.C. § 506(b):

> To the extent that an allowed secured claim is secured by property the value of which, after any recovery under subsection (c) of this section, is greater than the amount of such claim, there shall be allowed to the holder of such claim, interest on such claim, and any reasonable fees, costs or charges provided for under the agreement under which such claim arose.

A careful reading of Section 506(b) leads one correctly to conclude that it is a codification of the third exception to the general prohibition against allowing post-petition interest on an allowed secured claim filed in bankruptcy. *In re Churchfield*, 14 BCD 657 (E.D. Mich. 1986); 3 *Collier on Bankruptcy*, ¶ 506.05 at 506-37 n. 1 (15th ed. 1979); *contra, In re Loveridge Machine & Tool Co.*, 9 C.B.C. 2d 1329, 1332, n. 4. The third exception is that "the security (collateral) is sufficient to pay interest as well as the principal amount of the claim." As perceptively

pointed out by the Honorable Arthur J. Spector in *Churchfield, supra* at 658 (Bkcy. E.D. Mich. 1986), "Before there was a Bankruptcy Code there was a Bankruptcy Act." Accordingly, the analysis set forth in the pre-Code cases is controlling and must govern here.

The Seventh Circuit in *In re Kerber Packing Company*, 276 F.2d 245 (7th Cir. 1960), distinguished the Government's secured status as the result of a statutory lien from those creditors who held consensual liens.

> The third exception to the rule that interest does not accrue subsequent to filing provides protection to the creditor in his security which on liquidation produces a sufficient amount to satisfy the encumbrance and interest thereon. In the case of a mortgage or deed of trust, an *encumbrance is placed on the property voluntarily by the debtor as security for his deed after agreement with the creditor.* By this act the debtor authorizes not only the satisfaction of the deed out of the sale of the particular property but agrees to the payment of any deficiency that might arise after the sale and that other property he may own may be subjected to execution for payment of a deficiency judgment.
>
> This exception has been recognized by the courts to the extent of allowing post-bankruptcy interest to *creditors who are deemed to have bargained for collateral to secure not only the principal obligation but the interest thereon as well.* Usually the allowance has been in cases involving either mortgages, deeds of trust, bonds secured by collateral or a vendor's lien on a particular chattel and involving liens upon specific property of the bankrupt growing out of a contract between him and the creditor. (Emphasis added).

276 F.2d at 247. *Kerber* denied the IRS' request for post-petition interest in accord with the decisions of the Fourth, Ninth and Tenth Circuits.

Best Repair Co., 789 F.2d 1080 (4th Cir. 1986) is wrongly decided. It completely ignores the pre-Code cases on this issue and ascribes undue import to the word "any", which is no more than mere surplusage.

Section 506(b) is not clear, is not susceptible of any one interpretation, and does not have one "natural meaning".

Confronted with the identical issue now before this Court in *In re Churchfield*, 14 BCD at 658, the Honorable Arthur J. Spector respectfully disagreed with the Fourth Circuit's conclusion that Section 506(b) contains "plain terms" which compel the result it reached.

> Not being an authority on English grammar punctuation, we find that the words and punctuation of the Statute are hopelessly ambiguous, and so move on to analyze their meaning through examination of legislative intent, which even the Fourth Circuit believed was necessary and appropriate.

Churchfield, supra at 658.

The legislative intent clearly did not change existing case law.

The Notes of Committee on the Judiciary, Senate Report No. 95-989 state:

> Subsection (b) *codifies current law* by entitling a creditor with an oversecured claim to any reasonable fees (including attorney's fees), costs, or charges provided under the *agreement under which the claim arose.*" (Emphasis added).

This language is repeated in the Legislative Statements found in the Historical and Revision Notes.

> Section 506(b) of the House amendment adopts language contained in the Senate amendment and rejects language contained in H.R. 8200 as passed by the House. *If the security agreement between the parties provides for attorneys' fees*, it will be enforceable under Title 11, notwithstanding contrary law, and is recoverable from the collateral after any recovery under 506(c).

Legislative history does not indicate that by enacting Section 506(b) Congress affirmatively intended to expand the third exception to the general prohibition against paying post-petition interest on pre-petition secured claims to include nonconsensual tax liens.

> Pre-Bankruptcy Code precedent more strongly supports the latter view (IRS not entitled to post-petition interest on secured tax claim), and there is no evidence in the legislative history of 26 U.S.C. 6621 of Congressional intent to change that result.

3 *Collier on Bankruptcy*, § 506.05, p. 506-40.

In the face of the confusing commas, Section 506(b)'s ambiguity, and the absence of any indication whatsoever that Congress intended, considered, or even contemplated changing the case law which preceded enactment of Section 506(b), pre-Code cases should continue to govern.

The Court of Appeals for the Sixth Circuit correctly rejected the reasoning in *Best Repair*, *supra* in concluding that the placement of a comma and the inclusion of the words "and any" do not evince an intention to reject the well-established judicially created concept. As stated by

that court "the admitted lack of legislative history on this point lends further credence to [its] position. If Congress intended to depart from pre-Code law with respect to only this one portion of Section 506(b), . . . such an intent must be expressed explicitly and not through the ambiguous use of a comma . . . ." *In re Ron Pair Enterprises, Inc.*, 828 F.2d 367 (6th Cir. 1987).

Since the issuance of the Sixth Circuit's decision, the District Court in *Nevada Environmental Landfill*, 16 BCD 1248 (D. NV. 1987) similarly rejected the erroneous reasoning in *Best Repair* holding that current bankruptcy law further supports the distinction between consensual and non-consensual items and affirming that pre-Code bankruptcy law prohibiting post-petition interest on non-consensual liens has not been altered by the language of Section 506(b).

Finally, in *United Savings Association of Texas v. Timbers of Inwood Forest Associates, Ltd.*, 56 USLW 4107 (January 20, 1988) the United States Supreme Court rejected claims of undersecured creditors for post-petition interest on their claims. This Court stated that Section 506(b) merely codifies pre-Code bankruptcy law. Acknowledging the pre-Code rule denying such interest, the Supreme Court stated that had Congress nevertheless meant to give undersecured creditors interest on the value of their collateral it would have said so plainly in Section 506(b). *See United Savings Association of Texas v. Timbers of Inwood Forest Associates, Ltd.*, 56 USLW 4107 at 4109.

As the Supreme Court stated so recently in *Timbers of Inwood:*

> Such a major change in the existing rules would not likely have been made without specific provision in the text of the statute, c.f. *Kelly v. Robinson*, 479 U.S. —, — (1987); it is most improbable that it would have been made without even any mention in the legislative history.

United Savings Association of Texas, supra at 4109.

The issue here is whether 11 U.S.C. Section 506(b) applies to pre-petition non-consensual tax lien claims so as to permit interest on those claims to continue to accure after the filing of the bankruptcy petition until confirmation of the Debtor's Plan. Section 506(b) is a codification of the third exception to the general rule prohibiting such post-petition interest on a pre-petition non-consensual tax lien claim. The Section's legislative history is silent as to how Congress intended to deal with the payment of such interest and there is no indication that Congress intended to overrule prior, virtually unanimous, case law on this point. As recognized by the United States Supreme Court, silence is dangerous when one is attempting to overrule judicially created concepts. *Watt v. Alaska*, 451 U.S. 259 (1981). If Congress intends for legislation to change the interpretation of the judicially created concept, it makes that intent specific. *Mid Atlantic National Bank v. New Jersey*, 474 U.S. — (1986).

———o———

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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